Report

of the

Examination of

Partners Mutual Insurance Company

Waukesha, Wisconsin

As of December 31, 2004

TABLE OF CONTENTS

State of Wisconsin / OFFICE OF THE COMMISSIONER OF INSURANCE

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Jorge Gomez, *Commissioner*

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November 4, 2005

Honorable Jorge Gomez
Commissioner of Insurance
State of Wisconsin
125 South Webster Street
Madison, Wisconsin 53702

Commissioner:

In accordance with your instructions, a compliance examination has been made of the affairs and financial condition of:

PARTNERS MUTUAL INSURANCE COMPANY
Waukesha, Wisconsin

and this report is respectfully submitted.

I. INTRODUCTION

The previous examination of Partners Mutual Insurance Company (the company) was conducted in 2000 as of December 31, 1999. The current examination covered the intervening period ending December 31, 2004, and included a review of such 2005 transactions as deemed necessary to complete the examination.

The examination consisted of a review of all major phases of the company's operations, and included the following areas:

History
Management and Control
Corporate Records
Conflict of Interest
Fidelity Bonds and Other Insurance
Employees' Welfare and Pension Plans
Territory and Plan of Operations
Growth of Company
Reinsurance
Financial Statements
Accounts and Records
Data Processing

Emphasis was placed on the audit of those areas of the company's operations accorded a high priority by the examiner-in-charge when planning the examination. Special attention was given to the action taken by the company to satisfy the recommendations and comments made in the previous examination report.

The section of this report titled "Summary of Examination Results" contains comments and elaboration on those areas where adverse findings were noted or where unusual situations existed. Comment on the remaining areas of the company's operations is contained in the examination work papers.

The company is annually audited by an independent public accounting firm as prescribed by s. Ins 50.05, Wis. Adm. Code. An integral part of this compliance examination was the review of the independent accountant's work papers. Based on the results of the review of these work papers, alternative or additional examination steps deemed necessary for the completion of this examination were performed. The examination work papers contain documentation with respect to the alternative or additional examination steps performed during the course of the examination.

Independent Actuary's Review

An independent actuarial firm was engaged under a contract with the Office of the Commissioner of Insurance. The actuary reviewed the adequacy of the company's loss and loss adjustment expense reserves. The actuary's results were reported to the examiner-in-charge. As deemed appropriate, reference is made in this report to the actuary's conclusion.

II. HISTORY AND PLAN OF OPERATION

The company was organized in 1931, as Badger State Casualty Company, Limited Mutual. In February 1992, with approval of the company's policyholders, the company changed its name to Partners Mutual Insurance Company.

In 2004, the company wrote direct premium in the following states:

Wisconsin	$22,663,167	63.5%
Michigan	7,139,638	20.0
Iowa	5,868,553	16.5
Total	$35,671,358	100.0%

The company is licensed in Wisconsin, Michigan, and Iowa. The major products marketed by the company include auto physical damage, private passenger auto, homeowner's multi peril, commercial multi peril, and worker's compensation. The major products are marketed through 1,238 agents at 226 agencies in Iowa, Michigan, and Wisconsin.

The following table is a summary of the net insurance premiums written by the company in 2004. The growth of the company is discussed in the "Financial Data" section of this report.

Line of Business	Direct Premium	Reinsurance Assumed	Reinsurance Ceded	Net Premium
Fire	$ 174,797	$0	$ 24,683	$ 150,113
Allied lines	106,723		14,964	91,758
Homeowner's multiple peril	7,960,706		1,120,791	6,839,915
Commercial multiple peril	4,924,442		719,637	4,204,805
Inland marine	1,020,173		144,069	876,105
Earthquake	42		4	38
Worker's compensation	2,104,288		287,136	1,817,152
Other liability - occurrence	695,306		470,779	224,527
Private passenger auto liability	8,761,538		1,515,219	7,246,319
Commercial auto liability	1,269,641		319,289	950,351
Auto physical damage	8,653,703		177,423	8,476,280
Total All Lines	$35,671,358	$0	$4,793,996	$30,877,363

III. MANAGEMENT AND CONTROL

Board of Directors

The board of directors consists of nine members. Three directors are elected annually to serve a three-year term. Officers are elected at the board's annual meeting. The board members currently receive an annual retainer of $4,500 and a fee for attending each regular quarterly board meeting of $750 for serving on the board.

Currently the board of directors consists of the following persons:

Name and Residence	Principal Occupation	Term Expires
John A. Archer Milwaukee, WI	Retired Vice President, Schlitz Brewery	2006
Charles R. Ewert Brookfield, WI	Chairman of the Board Partners Mutual Insurance Company	2007
Mark H. Ewert Brookfield, WI	Executive VP and COO Partners Mutual Insurance Company	2006
Richard C. Ewert Brookfield, WI	President and CEO Partners Mutual Insurance Company	2008
Dean K. Harder Brookfield, WI	President and CEO, Harder Funeral Homes	2007
Paul R. Haut Brookfield, WI	President, W. Haut Specialty Co.	2006
Michael N. Herro Waukesha, WI	President and CEO, Geo-Synthetics, Inc.	2008
Reuben W. Peterson Bayside, WI	Attorney at Law Borgelt, Powell, Peterson & Frauen	2007
John A. Seefeldt* Green Bay, WI	Retired Port Director, City of Green Bay	2008
Mark F. Roethle** Wauwatosa, WI	President, Streff Advertising Inc.	2008

* John A. Seefeldt retired from the board effective November 1, 2005.

** Mark F. Roethle was appointed to the board effective November 17, 2005.

Officers of the Company

The officers serving at the time of this examination are as follows:

Name	Office	2004 Compensation
Richard C. Ewert	President	$123,344
Mark H. Ewert	Executive Vice President	91,075
Gregory E. Bergner	Secretary	95,034
John H. Klug	Treasurer	101,021
Neil L. Neff*	Vice President Marketing	81,069
Kenneth D. Shea	Vice President Claims	91,807

* Not included on the 2004 Report of Executive Compensation.

Committees of the Board

The company's bylaws allow for the formation of certain committees by the board of directors. The committees at the time of the examination are listed below:

Investment Committee
Richard C. Ewert, Chair
John A. Archer
Charles R. Ewert

Building Committee
Mark H. Ewert, Chair
Charles R. Ewert
Richard C. Ewert
Michael N. Herro

Salary Committee
John Seefeldt, Chair
John A. Archer
Richard C. Ewert
Paul R. Haut

Nominating Committee
Reuben W. Peterson, Chair
Richard C. Ewert
Dean K. Harder
John A. Seefeldt

IV. REINSURANCE

The company's reinsurance portfolio and strategy is described below. A list of the companies that have a significant amount of reinsurance in force at the time of the examination follows. The contracts contained proper insolvency provisions.

Ceding Contracts

1.	Type:	Property per Risk Excess of Loss
	Reinsurers:	Employers Reinsurance Corporation
	Scope:	All Property Business
	Commissions:	None
	Effective date:	January 1, 2004
	Termination:	By mutual consent or by either party on any January 1 with 90 days advance notice by registered mail.
	a. First Layer Retention:	$120,000 each risk, each occurrence
	Coverage:	100% of loss each risk involved in each occurrence excess of $120,000, subject to limits of $295,000 each risk involved in each occurrence and $885,000 all risks involved in each occurrence.
	Premium:	7.62% of net premium income
	b. Second Layer Retention:	$415,000 each risk, each occurrence
	Coverage:	100% of loss each risk involved in each occurrence excess of $415,000, subject to limits of $1,585,000 each risk involved in each occurrence and $3,170,000 all risks involved in each occurrence.
	Premium:	1.40% of net premium income
	c. Third Layer Retention:	$2,000,000 each risk, each occurrence
	Coverage:	100% of loss each risk involved in each occurrence excess of $2,000,000, subject to limits of $1,000,000 each risk involved in each occurrence and $2,000,000 all risks involved in each occurrence.
	Premium:	1.00% of net premium income

2.	Type:	Property Catastrophe
	Reinsurer:	Employers Reinsurance Corporation
	Scope:	All Property Business (except Umbrella)
	Commissions	None
	Effective date:	January 1, 1997, as amended
	Termination:	By mutual consent or by either party on any January 1 with 90 days advance notice by registered mail.
	Retention:	Part I: As respects each occurrence, an amount equal to $600,000, plus 5% of loss each occurrence excess of the applicable retention. Part II: The sum of the retention and the reinsurance under Part I for each occurrence. Part III: <u>Applicable to Winter Storms Only</u>—150% of the retention under Part I plus 5% of loss in excess of the applicable retention.
	Coverage:	Part I: 95% of loss each occurrence excess of the applicable retention subject to limits of 95% of $2,000,000 any one occurrence and 95% of $4,000,000 all occurrences taking place during any one calendar year. Part II: 100% of loss each occurrence excess of the applicable retention subject to limits of 100% of $4,000,000 any one occurrence and 100% of $8,000,000 all occurrences taking place during any one calendar year. Part III: <u>Applicable to Winter Storms Only</u>—95% of loss excess of the applicable retention subject to limits of 95% of $2,000,000 in the aggregate for all loss taking place during any one winter storm period. Provided, however, that the reinsurer's liability under Parts I and III combined shall not exceed 95% of $4,000,000 all occurrences during any one calendar year. Reinstatement of Indemnity: Each payment of loss reduces the amount of indemnity thereunder by the sum paid, but any amount of indemnity so reduced is hereby reinstated from the moment of the occurrence producing the loss, so that the amount of indemnity shall at all times remain 95% of $2,000,000 as respects Part I, and 100% of $4,000,000 as respects Part II, but the liability shall never exceed 95% of $4,000,000 as respects Part I, and 100% of $8,000,000 as respects Part II as respects all occurrences taking place during any one calendar year.

Premium:		Premium Rate	Annual Minimum Premium
	Part I:	2.748%	$263,006
	Part II:	1.810%	$173,232
	Part III:	Included in Part I	

Reinstatement Premium—On pro rata basis (as to fraction of the reinsurance limit so reinstated), the greater of the full reinsurance premium or the minimum reinsurance premium.

3. Type: Liability Excess

Reinsurer: Employers Reinsurance Corporation

Scope: All Casualty Business (except Umbrella and Auto Physical Damage)

Commissions: None

Effective date: January 1, 1997, as amended

Termination: By mutual consent or by either party on any January 1 with 90 days advance notice by registered mail.

Retention: First Layer: $120,000 each occurrence.

Second Excess: 10% of extra contractual loss subject to a limit of $100,000 each occurrence which exceeds the applicable retention and reinsurance limit under the first liability excess coverage.

Coverage: First Excess: $1,000,000 excess of $120,000 per occurrence except:

(1) $10,000 excess of $120,000 for medical payments;
(2) $20,000 excess of $120,000 for automobile death and disability;
(3) $100,000 excess of $120,000 for blanket position bonds;
(4) $300,000 excess of $120,000 for garage keepers legal liability and sexual misconduct;
(5) $400,000 excess of $120,000 for general liability on dealer's automobile physical damage
(6) $500,000 excess of $120,000 for commercial blanket bonds;
(7) $2,000,000 excess of $120,000 for benefits prescribed under the Automobile Accident Reparations Act of any state (as respects benefits under the Automobile Accident Reparations Act of the State of Michigan, loss shall include no amount greater than the per each occurrence retention set by the Michigan Catastrophic Claims Association if indemnity is afforded the company by the Catastrophic Claims Association with respect to such occurrence);
(8) $5,000,000 excess of $120,000 for worker's compensation and employers' liability

		Second Excess: 90% of contractual losses up to $1,000,000 each occurrence. Extra contractual loss is defined as punitive, exemplary or corresponding damages.
	Premium:	First Excess: 13.50% of net premium income Second Excess: 0.30% of net premium income
4.	Type:	Basket Reinsurance Agreement
	Reinsurer:	Employers Reinsurance Corporation
	Scope:	All property and liability lines of business written by the company
	Commissions	None
	Effective date:	January 1, 2004
	Termination:	By mutual consent or by either party on any January 1 with 90 days advance notice by registered mail.
	Retention:	$120,000 per occurrence regardless of number of claims arising from any one occurrence.
	Coverage:	$120,000 excess of $120,000 on any one risk, as chosen by the reinsured, per occurrence.
	Premium:	Reinsurance premiums paid under the property per risk first excess of loss and liability excess reinsurance agreement shall be deemed to include reinsurance premiums for this coverage.
5.	Type:	Equipment Breakdown Coverage
	Reinsurer:	Factory Mutual Insurance Company
	Scope:	Commercial multiple-peril policies with equipment breakdown endorsements and equipment breakdown policies covered under the company's commercial multiple-peril program.
	Commissions	30.0%
	Effective date:	July 1, 2004
	Termination:	By mutual consent or by either party on April 1, July 1, October 1 or January 1 with 180 days notice by registered mail.
	Retention:	None
	Coverage:	$5,000,000 on any one risk
	Premium:	100% share of written premium, remitted quarterly

6.	Type:	Umbrella and Commercial Excess Pro Rata
	Reinsurer:	Employers Reinsurance Corporation
	Scope:	Personal and commercial umbrella policies; and excess coverage for liability other than automobile policies, commercial automobile policies, businessowners policies, and contractors businessowners policies.
	Commissions	30.0%
	Effective date:	September 1, 1993, as amended
	Termination:	By mutual consent or by either party on any January 1 with 90 days advance notice by registered mail.
	Retention:	None
	Coverage:	100% to a maximum of $2,000,000 for umbrella policies and $1,000,000 excess of $1,000,000 for all policies other than umbrella.
	Premium:	Personal and commercial umbrella policies—pro rata share of net premium income. Liability other than automobile and businessowners other than excess contractors businessowners—5% of the first $1,000,000 premium with a minimum of $50 per policy. Contractors businessowners—16% of the first $1,000,000 premium with a minimum of $130 per policy. Commercial automobile (heavy trucks and tractors)—17% of the first $1,000,000 premium with a minimum of $100 per unit. Commercial automobile (units other than heavy trucks and tractors)—14% of the first $1,000,000 premium with a minimum of $35 per unit.

The company has an indemnity agreement with Employers Reinsurance Corporation (ERC) effective January 1, 1984, amended on January 14, 1997. In the event of the company's insolvency, the agreement provides for ERC to pay physical damage insurance claims on fire and other hazard insurance policies directly to the mortgagee. This agreement applies to only those policies which include an endorsement referencing the agreement. The endorsement is issued at the request of the mortgagee. ERC, in effect, becomes the direct insurer of policies carrying the referenced endorsement in the event of the company's insolvency.

The company utilizes ERC and Everest Re for facultative coverage on selected policies.

The company is a member of the Michigan Catastrophic Claims Association (MCCA), which provides indemnification for 100% of ultimate losses sustained under personal protection coverage in excess of $375,000 in each loss occurrence. Membership is a condition of the company's authority to transact insurance in Michigan.

V. FINANCIAL DATA

The following financial statements reflect the financial condition of the company as reported to the Commissioner of Insurance in the December 31, 2004, annual statement. Also included in this section are schedules that reflect the growth of the company, NAIC Insurance Regulatory Information System (IRIS) ratio results for the period under examination, and the compulsory and security surplus calculation. Adjustments made as a result of the examination are noted at the end of this section in the area captioned "Reconciliation of Surplus per Examination."

Partners Mutual Insurance Company
Assets
As of December 31, 2004

	Assets	Nonadmitted Assets	Net Admitted Assets
Bonds	$31,247,335	$	$31,247,335
Stocks:	1,556,860		1,556,860
Common stocks			
Cash	(56,988)		(56,988)
Receivable for securities	66,701		66,701
Investment income due and accrued	387,160		387,160
Premiums and considerations:			
Uncollected premiums and agents' balances in course of collection	1,486,237	5,133	1,481,105
Deferred premiums, agents' balances, and installments booked but deferred and not yet due	3,723,266		3,723,266
Reinsurance:			
Amounts recoverable from reinsurers	230,489		230,489
Current federal and foreign income tax recoverable and interest thereon	2,725		2,725
Net deferred tax asset	1,359,499	294,786	1,064,713
Electronic data processing equipment and software	367,132	289,965	77,167
Furniture and equipment, including health care delivery assets	31,238	31,238	
Write-ins for other than invested assets:			
Miscellaneous receivables	12,659	8,744	3,915
Cash surrender value life insurance	60		60
Total Assets	$40,414,373	$629,865	$39,784,507

Partners Mutual Insurance Company
Liabilities, Surplus, and Other Funds
As of December 31, 2004

Losses		$ 9,349,574
Loss adjustment expenses		1,815,978
Commissions payable, contingent commissions, and other similar charges		935,260
Other expenses (excluding taxes, licenses, and fees)		818,834
Taxes, licenses, and fees (excluding federal and foreign income taxes)		241,742
Current federal and foreign income taxes		183,959
Unearned premiums		11,780,765
Advance premium		537,474
Dividends declared and unpaid:		
Policyholders		91,000
Ceded reinsurance premiums payable (net of ceding commissions)		710,921
Amounts withheld or retained by company for account of others		12,450
Remittances and items not allocated		229,492
Write-ins for liabilities:		
Miscellaneous payables		3,315
Payable for operating software		130,688
Payable for agent's incentive		17,254
Total Liabilities		26,858,704
Write-ins for special surplus funds:		
Guaranty funds	$ 1,000,000	
Unassigned funds (surplus)	11,925,803	
Surplus as Regards Policyholders		12,925,803
Total Liabilities and Surplus		$39,784,507

Partners Mutual Insurance Company
Summary of Operations
For the Year 2004

Underwriting Income		
Premiums earned		$29,266,252
Deductions:		
Losses incurred	$14,274,749	
Loss expenses incurred	2,664,992	
Other underwriting expenses incurred	10,780,262	
Total underwriting deductions		27,720,003
Net underwriting gain or (loss)		1,546,249
Investment Income		
Net investment income earned	1,014,602	
Net realized capital gains or (losses)	160,037	
Net investment gain or (loss)		1,174,639
Other Income		
Net gain or (loss) from agents' or premium balances charged off	(14,022)	
Finance and service charges not included in premiums	283,273	
Write-ins for miscellaneous income:		
Net gain or (loss) on sale of ledger assets	(5,266)	
Total other income		263,986
Net income (loss) before dividends to policyholders and before federal and foreign income taxes		2,984,875
Dividends to policyholders		155,193
Net income (loss) after dividends to policyholders but before federal and foreign income taxes		2,829,682
Federal and foreign income taxes incurred		1,035,282
Net Income		$ 1,794,400

Partners Mutual Insurance Company
Cash Flow
For the Year 2004

Premiums collected net of reinsurance			$30,521,890
Net investment income			1,602,099
Miscellaneous income			263,986
Total			32,387,974
Benefit- and loss-related payments		$14,308,472	
Commissions, expenses paid, and aggregate write-ins for deductions		13,119,256	
Dividends paid to policyholders		172,193	
Federal and foreign income taxes paid (recovered)		1,721,000	
Total deductions			29,320,920
Net cash from operations			3,067,054
Proceeds from investments sold, matured, or repaid:			
Bonds	$ 8,655,634		
Stocks	12,208,847		
Total investment proceeds		20,864,481	
Cost of investments acquired (long-term only):			
Bonds	11,039,795		
Stocks	12,365,057		
Total investments acquired		23,404,852	
Net cash from investments			(2,540,371)
Cash from financing and miscellaneous sources:			
Other cash provided (applied)		(451,216)	
Net cash from financing and miscellaneous sources			(451,216)
Reconciliation			
Net change in cash and short-term investments			75,467
Cash and short-term investments, December 31, 2003			(132,455)
Cash and short-term investments, December 31, 2004			$ (56,988)

Partners Mutual Insurance Company
Compulsory and Security Surplus Calculation
December 31, 2004

Assets		$39,784,507
Less liabilities		26,858,704
Adjusted surplus		12,925,803
Annual premium:		
Lines other than accident and health	$30,877,363	
Factor	20%	
Compulsory surplus (subject to a minimum of $2 million)		6,175,473
Compulsory surplus excess (or deficit)		$ 6,750,330
Adjusted surplus (from above)		$12,925,803
Security surplus: (140% of compulsory surplus, factor reduced 1% for each $33 million in premium written in excess of $10 million, with a minimum factor of 110%)		8,645,662
Security surplus excess (or deficit)		$ 4,280,141

Partners Mutual Insurance Company
Reconciliation and Analysis of Surplus
For the Five-Year Period Ending December 31, 2004

The following schedule is a reconciliation of total surplus during the period under examination as reported by the company in its filed annual statements:

	2004	2003	2002	2001	2000
Surplus, beginning of year	$10,985,428	$ 8,667,938	$8,552,728	$ 9,101,033	$10,047,833
Net income	1,794,400	1,664,708	72,704	(1,107,012)	(1,003,199)
Net unrealized capital gains or (losses)	487,040	106,712	21,721	(9,069)	(27,853)
Change in net deferred income tax	(97,553)	25,152	20,555	461,011	
Change in non-admitted assets	(243,512)	520,919	230	(698,413)	84,252
Cumulative effect of changes in accounting principles				805,179	
Surplus, end of year	$12,925,803	$10,985,428	$8,667,938	$ 8,552,728	$ 9,101,033

Partners Mutual Insurance Company
Insurance Regulatory Information System
For the Five-Year Period Ending December 31, 2004

The company's NAIC Insurance Regulatory Information System (IRIS) results for the period under examination are summarized below. Unusual IRIS results are denoted with asterisks and discussed below the table.

	Ratio	2004	2003	2002	2001	2000
#1	Gross Premium to Surplus	276.0%	275.0%	334.0%	304.0%	254.0%
#2	Net Premium to Surplus	239.0	241.0	296.0	273.0	228.0
#3	Change in Net Writings	16.0	3.0	10.0	12.0	1.0
#4	Surplus Aid to Surplus	0.0	0.0	0.0	0.0	0.0
#5	Two-Year Overall Operating Ratio	90.0	94.0	101.0*	105.0*	100.0*
#6	Investment Yield	3.2*	4.1*	5.1	5.7	6.0
#7	Change in Surplus	17.0	24.0	2.0	(3.0)	(6.0)
#8	Liabilities to Liquid Assets	70.0	72.0	76.0	78.0	71.0
#9	Agents' Balances to Surplus	11.0	13.0	14.0	14.0	0.0
#10	One-Year Reserve Development to Surplus	(15.0)	(8.0)	1.0	(17.0)	(6.0)
#11	Two-Year Reserve Development to Surplus	(13.0)	(3.0)	(16.0)	(18.0)	(16.0)
#12	Estimated Current Reserve Deficiency to Surplus	1.0	6.0	10.0	(1.0)	(15.0)

The company has an exceptional ratio in #6, Investment Yield, for the last two years. This exception is largely due to the decline in interest rates and that the company mainly invests in tax-exempt bonds which in recent years have had a lower yield. The company's "two-year overall operating ratio" (ratio #5) for 2000 through 2002 was exceptional mainly due to some unusually severe storms resulting in numerous claims in those years.

Growth of Partners Mutual Insurance Company

Year	Admitted Assets	Liabilities	Surplus As Regards Policyholders	Net Income
2004	$39,784,507	$26,858,704	$12,925,803	$ 1,794,400
2003	36,195,979	25,210,552	10,985,428	1,664,708
2002	32,367,550	23,699,612	8,667,938	72,704
2001	30,633,226	22,080,497	8,552,729	(1,107,012)
2000	29,126,836	20,025,803	9,101,033	(1,003,199)
1999	29,759,535	19,711,702	10,047,833	987,085

Year	Gross Premium Written	Net Premium Written	Premium Earned	Loss And LAE Ratio	Expense Ratio	Combined Ratio
2004	$35,671,358	$30,877,363	$29,266,252	57.9%	34.1%	92.0%
2003	30,261,132	26,504,903	25,923,515	60.5	34.6	95.1
2002	28,985,818	25,666,522	25,055,458	71.2	31.8	103.0
2001	26,014,374	23,332,253	21,832,023	76.4	34.2	110.6
2000	23,077,806	20,750,677	20,280,551	73.6	38.2	111.8
1999	22,728,075	20,556,956	20,759,705	65.6	35.0	100.6

The company has experienced surplus growth over the past two years of 49%. Premium growth has been steady over the five-year period under examination and is attributable to the company's successful marketing strategy through their network of independent agencies. The company has reduced its loss ratio over the last four-year period, thus contributing to a positive net income for 2002-2004.

Reconciliation of Surplus per Examination

No adjustments were made to surplus as a result of the examination. The amount of surplus reported by the company as of December 31, 2004, is accepted.

VI. SUMMARY OF EXAMINATION RESULTS

Compliance with Prior Examination Report Recommendations

There were four specific comments and recommendations in the previous examination report. Comments and recommendations contained in the last examination report and actions taken by the company are as follows:

1. Premium—Therefore, it is recommended that the company continue to develop a system under which the premium will be recognized as of the effective date of the coverage in compliance with SSAP 53.

   Action—Compliance.

2. Aggregate Write-ins for other than Invested Assets—It is recommended that the company properly report travel advances and other prepaid items (Deposits for Agency Promotional Contests) as nonadmitted assets in compliance with the NAIC Annual Statement Instructions Property and Casualty.

   Action—Compliance.

3. Other Expenses—It is recommended that the company discontinue its practice of offsetting accounts payable with prepaid rent, and properly report prepaid rent as a nonadmitted asset in accordance with NAIC Annual Statement Instructions Property and Casualty.

   Action—Compliance.

4. Underwriting—It is recommended that the company discontinue charging service fees for installment billing plans on worker's compensation insurance policies in order to comply with s. 626.25 (1), Wis. Stat

   Action—Compliance.

Summary of Current Examination Results

This section contains comments and elaboration on those areas where adverse findings were noted or where unusual situations existed. Comment on the remaining areas of the company's operations is contained in the examination work papers.

Executive Compensation

The 2004 Report of Executive Compensation to the commissioner did not include all appropriate individuals. According to s. 611.63 (4), Wis. Stat., companies are to report to the commissioner, on an annual basis, all direct and indirect remuneration for services, including retirement and other deferred compensation benefits and stock options, paid or accrued each year for the benefit of each director and each officer and employee whose remuneration exceeds the amount established by the commissioner. In this case, the company included individuals on the 2004 Report of Executive Compensation based on salary alone. It is recommended that the company correctly include all appropriate individuals on the Report on Executive Compensation in compliance with s. 611.63 (4), Wis. Stat.

Information Technology

The company takes copies of its AS400 backup tapes off-site about once a week. Network tapes are not taken off-site. To ensure that the company has a current backup of its tapes, the company should be taking them off-site more frequently. Best practices would indicate backups should be taken off-site nightly. However, due to the size of the company and the risk, twice a week would be acceptable. In addition, the tapes are stored in a filing cabinet when off-site. The filing cabinet is not locked or fireproof. To ensure a reasonable level of security of the tapes, they should be stored in a locked, fireproof container when stored off-site. It is recommended that the company establish a procedure where backup tapes for the network and AS400 are rotated off-site at least twice a week.

The company's disaster recovery plan was developed in 1994 through the use of a template. From a review of the plan, it appears that most of the plan has not been updated since it was created. The plan indicated that it would be updated annually. To be effective, disaster plans should be periodically reviewed, updated, and tested at least annually. The following was identified in the plan: critical vendors in one section of the plan were listed without phone numbers, critical supplies were not listed, detailed instructions in restoring the company's IT operations were not included, and functional plans included action tasks which required that detailed plans be determined during the disaster. The benefit of a disaster plan is to have key people identified, key supplies identified and stored off-site, and decisions, or at least the parameters of decisions, made prior to a disaster. It is recommended that the company review, update, and test its disaster recovery plan at least annually.

A review of employee’s IDs for the company's system identified that there were enabled IDs for individuals no longer with the company or for individuals who had no need for the ID to be active. In addition, the company does not have a formal periodic process to validate that the rights assigned to an ID are commensurate with the responsibilities associated with that ID. This could result in IDs having more rights than necessary to complete tasks. It is recommended that the company perform a formal periodic review of IDs to validate that all active IDs are authorized and that the access rights for an ID are limited to those necessary to perform their job including both network and application access.

The company's passwords for access to their network and AS400 are limited to four characters. One of the applications has a password minimum of one character. Considering the fact that the company's passwords do not have to be complex, four characters are inadequate and increase the potential that passwords would be compromised allowing unauthorized access. It is recommended that the company increase its minimum password length requirement to at least five characters.

Cash

A review of the cash disbursements found a claim check that was issued and cashed without a proper signature. It is recommended that cash disbursement procedures ensure that the claim check presentment is reviewed to verify proper signature approval exists.

The check stock in use is maintained under a printer in the claims area. This exposes the checks to being lost, damaged or stolen. It is recommended the company secure their check stock when not in use.

VII. CONCLUSION

Policyholders' surplus has increased from $10,047,833 as of year-end 1999, to $12,925,803 as of year-end 2004. This represents an increase of 28.7% during the period under examination, which is partially attributable to steady premium growth and reduction of the company's loss ratio during this time. Operating earnings have been profitable over the last three-year period under examination due to favorable weather conditions in the Midwest, continually good underwriting performances, and steady investment income.

The examination of Partners Mutual Insurance Company resulted in seven recommendations, no adjustment to surplus and no reclassifications. The recommendations pertain to the proper annual statement filing requirements relating to executive compensation, the company's disaster recovery plan and controls over the company's computer systems and cash.

VIII. SUMMARY OF COMMENTS AND RECOMMENDATIONS

1. Page 23 - Executive Compensation—It is recommended that the company correctly include all appropriate individuals on the Report on Executive Compensation in compliance with s. 611.63 (4), Wis. Stat.

2. Page 23 - Information Technology—It is recommended that the company establish a procedure where backup tapes for the network and AS400 are rotated off-site at least twice a week.

3. Page 24 - Information Technology—It is recommended that the company review, update, and test its disaster recovery plan at least annually.

4. Page 24 - Information Technology—It is recommended that the company perform a formal periodic review of IDs to validate that all active IDs are authorized and that the access rights for an ID are limited to those necessary to perform their job including both network and application access.

5. Page 24 - Information Technology—It is recommended that the company increase its minimum password length requirement to at least five characters.

6. Page 24 - Cash—It is recommended that cash disbursement procedures ensure that the claim check presentment is reviewed to verify proper signature approval exists.

7. Page 24 - Cash—It is recommended the company secure their check stock when not in use.

IX. ACKNOWLEDGMENT

The courtesy and cooperation extended during the course of the examination by the officers and employees of the company are acknowledged.

In addition to the undersigned, the following representatives of the Office of the Commissioner of Insurance, State of Wisconsin, participated in the examination:

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Thomas Janke	Insurance Examiner
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Respectfully submitted,

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